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No. 91-886

In The

Supreme Court of the United States

October Term, 1991

BOB REVES, ROBERT H. GIBBS, and FRANCES GRAHAM, as Representatives of a Class of Note Holders,

Petitioners,

v.

ERNST & YOUNG,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF OF AMICUS CURIAE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS, IN SUPPORT OF PETITIONERS

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INTEREST OF THE AMICUS CURIAE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

The National Association of Insurance Commissioners ("the NAIC") is a voluntary unincorporated association comprised of the chief insurance regulatory officials with

principal responsibility for supervising the business of insurance in the states, territories, and insular possessions of the United States. As stated in its constitution, the organization aims to help state officials achieve fundamental insurance regulatory objectives, among which is effective financial solvency regulation.

This objective has assumed special prominence in recent years as the failure of major insurers has left millions of policyholders holding worthless policies and annuities. The NAIC's members have found that their ability to identify a company in financial distress in time to avert failure requires that they receive complete and honest information about the financial condition of the companies they regulate. Fraud and other acts of dishonesty in reporting financial information frustrate this solvency regulatory process, whether the dishonesty is attributable to company owners and managers or independent consultants, such as auditors, actuaries and attorneys, all of whom are essential participants in the financial reporting process.

Where an insurance company's failure is the result of fraud or other dishonesty, the NAIC's members believe the perpetrators should be punished and, if possible, the victims—including the defrauded company and its policyholders—compensated by the wrongdoers. The members have found RICO, including both its criminal penalties and civil remedies, to be a strong and useful enforcement tool. Therefore, the NAIC, in assisting its members to fulfill the fundamental regulatory objective of effective solvency regulation, has a direct interest in assuring the continued availability of civil and criminal RICO as a vehicle for compensating its victims and for punishing dishonesty, whether perpetrated by company management or by independent entities and consultants.

The NAIC's members believe that the Eighth Circuit's interpretation of RICO's "participation" element shields independent entities and consultants from RICO liability, even where their conduct has been essential to the perpetration of an illegal scheme that has caused or concealed an insurance company's insolvency. To this end, the NAIC supports the position of the Petitioners in urging the reversal of the Eighth Circuit opinion. The parties have consented to the filing of this brief, and the consents are on file with the Clerk of the Court.

SUMMARY OF ARGUMENT

The Eighth Circuit held that an accounting firm that misrepresented its audit client as solvent when in fact it knew the client was insolvent could not be liable for a RICO violation, because an outside auditor does not "operate" or "manage" the client company, and therefore cannot participate, even indirectly, in the conduct of its affairs within the meaning of RICO, 18 U.S.C. §1962(c). But the key actors in successful frauds involving the illegal operation of insurance companies invariably include independent entities, such as insurance agencies, brokers and reinsurers, and consultants, such as accountants, actuaries and attorneys. Therefore, if the Eighth Circuit's holding is affirmed, these wrongdoers will be effectively immunized from RICO prosecution, even where their misconduct proximately caused injuries to insurance companies and their policyholders.

The holding should not, however, be affirmed. It ignores the plain language of RICO, which proscribes misconduct

by those who directly and *indirectly* participate in the conduct of a company's affairs, and so it is contrary to Congress's intent that the statute apply to independent third parties as well as company insiders; it eviscerates RICO as a weapon against fraudfeasors who happen not to be part of the inside management team; and it is not necessary for preventing frivolous RICO claims from clogging our courts.

Recent insurance company failures, caused or concealed by fraud and deceit in the operation of the failed companies and false financial reporting about the failed companies, have already cost the American public many billions of dollars. A congressional subcommittee studying whether the insurance industry will suffer a disaster in the 1990's of the same magnitude as the savings and loan disaster of the 1980's, recently encouraged responsible officials to pursue those—company insiders and independent entities and consultants alike—who commit frauds against insurance companies. Insurance officials charged with liquidating the estates of insolvent insurers have successfully used RICO to recover damages from both company insiders and outside entities and consultants on behalf of the insolvent insurers and their policyholders. The NAIC and its member state officials, therefore, urge that the Eighth Circuit's decision be reversed in order to preserve the scope of RICO as a forceful deterrent and remedial provision.

ARGUMENT

A federal jury found the accounting firm, Arthur Young & Co., guilty of acts of federal and state securities fraud in connection with its audits of a grain cooperative ("the Co-op"). The victims of the fraud were farmer-members of the Co-op, who lent it money on the strength of Arthur Young's representations—which turned out to be *mis*representations—about the Co-op's financial condition. The jury was not allowed, however, to consider whether Arthur Young also violated RICO, 18 U.S.C. §1962(c),[1] because the district court held that, as a matter of law, an auditor's involvement with its client does not constitute "participation" in the conduct of its client's affairs within the meaning of the statute. On review, the Eighth Circuit characterized Arthur Young's actions as "reprehensible," but affirmed the lower court's decision, because under its view, one who does not "operate" or "manage" the entity identified as the RICO enterprise cannot participate, even indirectly, in the conduct of its affairs within the meaning of section 1962(c). *Arthur Young & Co. v. Reves*, 937 F.2d 1310, 1324 (8th Cir. 1991).

If this decision is affirmed, it will render RICO useless as a tool for pursuing those whose illegal operation of insurance companies has ruined solid businesses, left policy-

[1] Section 1962(c) provides:

> It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

holders with worthless claims against insolvent companies, and imposed a multi-billion dollar burden on the American public.[2] For this reason, the NAIC and its member state insurance regulators join the petitioners in urging reversal of the Eighth Circuit decision.

A. The Illegal Operation of an Insurance Company Generally Requires the Culpable Involvement of Independent Entities and Consultants.

Insurance companies, the repositories of huge sums of money derived from policyholders' premium dollars, are attractive targets of fraud.[3] There are two typical configurations of fraud involving the illegal operation of insurance companies. In one, the company's assets are siphoned off, usually through affiliates, agents, and reinsurers. In the other, the company's insolvency is concealed so that it can continue to take in money by selling policies that later turn out to be of no value.

[2] A Congressional subcommittee ("the Dingell Committee") investigating the causes of insurance company insolvencies found that four recent failures—all of which the subcommittee attributed at least in part to fraud and deceit—would alone cost the public $5 billion. Staff of House Comm. on Energy and Commerce, 101st Cong. 2d Sess., "Failed Promises; Insurance Company Insolvencies" at 2-3 (Comm. Print 101-P 1990) [hereinafter cited as *Failed Promises*].

[3] As the Dingell Committee explained it:

> The business of insurance is uniquely suited to abuse by mismanagement and fraud. Making believable promises is a stock item in every con man's bag of tricks. The prepayment of large, often vast, sums of money with few restrictions lends itself naturally to monumental wasting of assets through greed, incompetence, and dereliction of duty. This combination of easy money based on easy promises makes the insurance industry an irresistible target for financial knaves and buccaneers.

Failed Promises at 3.

Most often, these frauds are perpetrated as the joint effort of company management or employees and third party wrongdoers, and result in bankrupting solvent companies or deepening an already existing insolvency. For example, the Dingell Committee concluded that the failure of Mission Insurance Company, one of the largest insurance company insolvencies in history, was fueled by the deceit of agents and reinsurers doing business with Mission; and that it was concealed by false financial reports filed with regulators by Mission and the auditors of Mission's parent. *Failed Promises* at 16-21.

This deceit was not unique to Mission. Many documented frauds against insurance companies involve third parties acting in concert with company managers to skim money through inflated commissions and fees.[4] Others involve fraudulent investments of policyholder premium dollars in sweetheart deals or non-performing loans;[5] and still others involve complex schemes with third parties in which sham reinsurance is used artificially to inflate policyholders' surplus.[6]

[4] *E.g., Curiale v. Peat, Marwick, Mitchell & Co.*, No. 2310/87 (N.Y. Sup. Ct. N.Y. Cty., Jan. 10, 1992) (alleged diversion of $10 million in excessive management fees; summary judgment denied); *State of Florida Department of Insurance v. Merrill Lynch*, No. 91-17911 (Circuit Ct. Duval Cty., Florida, filed Dec. 20, 1991) (liquidator's complaint alleging looting through excessive fees, compensation and illegal dividends, as well as fraudulent scheme to conceal insurer's insolvency).

[5] For example, the Dingell Committee singled out the "irresponsible junk bond practices" of First Executive Corporation. *Failed Promises* at 7.

[6] *Failed Promises* at 42 describes a sham reinsurance scheme that enabled Transit Casualty Company to lull regulators by reporting a stable surplus when in fact the company was insolvent by billions of dollars. *See also Levine v. American Federal Group, Ltd.*, Mealey's Insurance Insolvency, March 18, 1992 at C-1 (N.Y. App.Div. 1992) (dispute involving broker who allegedly placed reinsurance with a reinsurer known to be insolvent).

A goal of insurance regulation is detecting these frauds before they cause company failure. But most of the regulators' information about insurance companies comes from the companies themselves, primarily through detailed financial statements filed with the regulators at least annually. Thus, where the illegal scheme includes concealing a failing or insolvent financial condition through, for example, fraudulently underreported loss reserves or sham reinsurance, the regulators' ability to detect the fraud is dependent in the first instance on the honesty of persons who, in fact, are perpetrating and concealing it. Negligence and defalcations in financial reporting have prompted regulators to require companies to provide actuarial opinions on the adequacy of loss reserves and to obtain annual audits of their balance sheets and income statements from independent certified public accountants.[7] The regulatory purposes of these initiatives are obviously frustrated when consulting actuaries and independent auditors lend their prestige and knowingly join management's scheme to cover up an insurer's true financial condition.

B. Civil RICO Is a Tested and Successful Weapon in the Fight Against Fraudulent Operation of Insurance Companies.

The mail and wire fraud statutes have always been effective vehicles for criminally prosecuting those involved in the fraudulent operation of insurance companies.[8] What

[7] The so-called audit rule, which has been in force in some states since the 1970's, *e.g.*, 50 Ill. Admin. Code 925 (1975), was recently adopted as an amendment to the Annual Statement Instructions, and thereby made applicable in all states. Vol.IA 1991 *Proceedings of the NAIC* 319.

[8] *E.g.*, *United States v. Cosentino*, 869 F.2d 301 (7th Cir.), *cert. denied*, 492 U.S. 908 (1989) (criminal conviction for siphoning off

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was historically missing, however, were effective civil remedies for compensating the victims of the frauds—the companies and their policyholders. RICO has filled that gap.

The first civil RICO complaint on behalf of a defrauded insurance company, filed in 1981, is described in *Schacht v. Brown*, 711 F.2d 1343 (7th Cir.), *cert. denied*, 464 U.S. 1003 (1983). Schacht was the liquidator of Reserve Insurance Company, an insolvent Illinois property and casualty insurer faced with a $100 million deficit. He brought a RICO suit against the company's officers, directors, reinsurers, auditors and others. As the Seventh Circuit described it, the defendants were charged under 18 U.S.C. §1962(c) with participation in a "multifaceted, fraudulent scheme, which kept Reserve operating long past insolvency in a manner which resulted in enormous losses to the latter company." 711 F.2d at 1346. The scheme could not have succeeded without the help of the third party wrongdoers: the reinsurer, which (the complaint alleged), in exchange for a multimillion dollar fee, entered a financing transaction that was falsely presented on Reserve's financial statements as reinsurance; and the auditors who (allegedly) consented to the false and misleading presentation of the financing transaction in Reserve's financial state-

[8] *continued*

insurance company assets through affiliated broker affirmed); *United States v. Joyce*, 499 F.2d 9 (7th Cir.), *cert. denied*, 419 U.S. 1031 (1974) (affirming mail fraud conviction of schemers who persuaded people to place insurance with an under-capitalized insurance company and then siphoned off the premium dollars for personal use); *United States v. Kreimer*, 609 F.2d 126 (5th Cir. 1980) (affirming conviction where an insurance company was defrauded by agents who accepted secret fees and commissions for policies they wrote for the company).

ments and failed to disclose Reserve's insolvency. *Id.* at 1345.[9]

Other liquidators of insolvent insurers who have sued under RICO have also achieved recoveries on behalf of defrauded companies. As examples, the liquidator of Beacon Insurance Company recently obtained a multimillion dollar settlement of a RICO suit against a group of agents and brokers who, he claimed, defrauded Beacon into accepting imprudent risks for insufficient premiums. *See generally State of North Carolina ex rel. Long v. Alexander & Alexander*, 680 F.Supp. 746 (E.D.N.C. 1988) and No. 86-1247-Civ.-5 (E.D.N.C. Jan. 22, 1992) (dismissal order). And a jury ordered the majority shareholder of an insolvent Texas insurer to pay in excess of $1 million (trebled) in RICO damages for his participation in a scheme to siphon off company assets through excessive commission payments to an agency owned by the shareholder. *Durish v. Uselton*, Mealey's Insurance Insolvency, August 15, 1990 at D-1 (N.D. Texas 1990).[10]

[9] The Reserve litigation recently settled. *Stamp v. Brown*, No. 81 C 1475 (N.D. Ill., Feb. 20, 1992) (dismissal orders). By agreement of the parties the dollar amount of the settlement will be disclosed later this month.

[10] At least two other liquidators are presently pursuing RICO claims on behalf of an insolvent insurer. Last year the liquidator of the insolvent Coastal Insurance Company filed RICO claims against persons and entities who allegedly diverted premium dollars earmarked for Coastal to themselves. *Garamendi v. Harry O. Miller et al.*, No. BC007903 (Super. Ct. Los Angeles Cty., Calif., filed August 10, 1990); and *Gallinger et al. v. B.D. Owens et al.*, CV 91-1867 PHXWPC (D. Ariz., filed Nov. 25, 1991).

Several others have filed RICO claims that were dismissed as untimely or because of pleading deficiencies. *See Hunt v. American Bank & Trust Co. of Baton Rouge*, 783 F.2d 1011 (11th Cir. 1986) (RICO claims for siphoning off insurer's assets dismissed as time-barred); *Corcoran v. American Plan Corp.*, 886 F.2d 16 (2d Cir.

(Footnote continued on following page)

The success of these prosecutions is attributable to the availability of RICO. The liquidators' state remedies for fraud are burdened in ways RICO is not. These burdens include state law privileges, inapplicable in federal question cases, that protect the auditors of insurance companies from having to produce their workpapers, even when the auditors are sued for participation in schemes to defraud the audited company;[11] complicated and uneven state laws of contribution and joint and several liability that are inapplicable in RICO suits,[12] but may allow culpable defendants sued on state causes to avoid some or all liability;[13] and problems of service and venue presented

[10] *continued*

1989) (liquidator's RICO suit against persons and entities who allegedly looted two defunct New York insurers dismissed under the Second Circuit's rule that there is no mail fraud violation in the absence of a coalescence between the person deceived—there, the regulators—and the person injured—the insurance companies).

[11] For example, in Illinois an accountant is protected from producing its audit workpapers in discovery by the so-called "Accountant's Privilege," Ill.Rev.Stat. ch.111, ¶5533, which the auditor defendants unsuccessfully invoked in the Reserve Insurance Company RICO action. The same auditors were, however, successful in preventing access to the same workpapers by bank creditors of Reserve's holding company in their state law civil fraud suits. *LaSalle National Bank v. Arthur Andersen*, No. 82 L 17602 (Cir. Ct. Cook Cty., Ill., July 27, 1984) (order denying plaintiff access to audit workpapers due to state law accountant privilege).

[12] The courts that have considered the issue have all held that contribution is not available as to RICO liability. *Miller v. Affiliated Financial Corp.*, 624 F.Supp. 1003 (N.D.Ill. 1985); *Minpeco, S.A. v. Conticommodity Services, Inc.*, 677 F.Supp. 151 (S.D.N.Y. 1988); *Dept. of Economic Development v. Arthur Andersen & Co.*, 747 F.Supp. 922 (S.D.N.Y. 1990); and *cf., Fleischhauer v. Feltner*, 879 F.2d 1290 (6th Cir. 1989), *cert. denied*, 494 U.S. 1027 (1990) (RICO liability is joint and several).

[13] A total of twelve states have abolished joint and several liability, ten by statute—Arizona, Colorado, Connecticut, Idaho, In-

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by state law actions involving a complex scheme, wrongful conduct and injury spanning several states, and multiple defendants, which are pretermitted by RICO's liberal venue and nationwide service of process provisions.

C. The Court Should Adopt the Seventh Circuit's Definition of "Participate," Because It Is Consistent With the Meaning of the Plain Language of the Statute.

The successful civil RICO prosecutions brought by the Reserve, Beacon and Texas Fidelity liquidators would have been stillborn if they had been filed in the Eighth Circuit, where the rule is that one who does not "operate" or "manage" the entity identified as the RICO enterprise cannot participate, even indirectly, in the conduct of its affairs within the meaning of section 1962(c). *Arthur Young & Co. v. Reves, supra* 937 F.2d at 1324. Key actors in the schemes that ruined Reserve, Beacon and Texas Fidelity were accountants, outside consultants and other third party wrongdoers: in Reserve they included the company's auditors and reinsurers; in Beacon and Texas Fidelity they included brokers and agents.

These wrongdoers would have been excluded from the litigation and insulated from liability under the *Arthur Young* rule; and the liquidators would have been handicapped in their ability to discover, present and, of course, remedy the full scope of the illegal conduct. In fact, as

[13] *continued*
diana, Michigan, New Mexico, North Dakota, Utah and Wyoming; and two by judicial decision—Kansas and Oklahoma. In these states, a plaintiff may not seek to recover from one or more defendants for the entire injury caused as a result of tortious conduct, but can instead recover only from each defendant based on its proportionate liability.

a practical matter, where the RICO enterprise is a legitimate company, the Eighth Circuit rule immunizes all persons except company ownership and management from section 1962(c) liability.[14] In turn, the rule eviscerates RICO as an effective remedy for the victims of most frauds involving the illegal operation of insurance companies. This is an unfortunate and unnecessary result.

Section 1962(c) provides that it shall be unlawful for any person employed by or associated with an enterprise "to conduct or participate, directly or indirectly, in the conduct of [an] enterprise's affairs" through a pattern of racketeering activity. In its "operate" or "manage" construction of the participation element, the Eighth Circuit has ignored the disjunctive wording of the statute: "conduct *or* participate, directly or indirectly, in the conduct." By holding instead that a RICO defendant *must* conduct (defined as "operate" or "manage") the enterprise's affairs, it has read out of Congress's plain language the words "or participate, directly or indirectly in the conduct."

Other courts have not been so miserly in their reading of the statute, and as a result, in other circuits RICO has been available as a prosecutorial tool against all persons involved in enterprise crimes. As the Eleventh Circuit

[14] It does not appear that even artful and circumspect pleading can evade the force of the *Arthur Young* rule. In that case, for example, the plaintiffs had alleged the audit firm, in whose affairs the individual auditors had plainly participated, as a RICO enterprise. The district court held this was insufficient, because in its view the illegal acts charged were not "typical of the practice of these professionals," from which the court concluded that the affairs of the firm were not conducted "through" a pattern of racketeering activity. *Robertson v. White*, No. 85-2044 (W.D. Ark., Oct. 15, 1986) (granting various motions for summary judgment) Pet.App. at 72-3.

held in reversing a motion to dismiss an audit firm charged under section 1962(c) with participating in the affairs of its client, the alleged enterprise:

> It is not necessary that a RICO defendant participate in the management or operation of the enterprise. On its face, the statute requires only that the defendant "participate, directly or indirectly in the conduct of [the] enterprise's affairs. . . ." 18 U.S.C. § 1962(c). . . . Defendants argue that Congress intended to limit the reach of a civil RICO action by imposing a "conduct" requirement, *i.e.*, that defendant conducted or participated in the conduct of a RICO enterprise in a significant manner. This argument ignores the "directly or indirectly" language of § 1962(c).

Bank of America National Trust & Savings Association v. Touche Ross & Co., 782 F.2d 966, 970 (11th Cir. 1986).

The circuit with the most fully developed jurisprudence on the "participation" element of RICO is the Seventh. That court views the statute as sufficiently broad to encompass third party wrongdoers where: (1) they commit the racketeering acts; (2) their position in or relation with the enterprise facilitated commission of the acts, and (3) the acts had "some effect" on the enterprise. *United States v. Pieper*, 854 F.2d 1020, 1026 (7th Cir. 1988). As the Seventh Circuit has explained:

> The participation in the conspiracy of people who were not on the legitimate payroll of [the company] does not mean those people were not participating in its affairs. The nature of racketeering connections to an otherwise legitimate business suggests that elements outside a company may assist in obtaining the company's illegal goals.

United States v. Starnes, 644 F.2d 673, 679 (7th Cir.), *cert. denied*, 454 U.S. 826 (1981) (affirming the section 1962(c)

conviction of an arsonist hired by the corporate president to burn the enterprise/company's property). *See also United States v. Blackwood*, 768 F.2d 131 (7th Cir.), *cert. denied*, 474 U.S. 1020 (1985) (affirming the section 1962(c) conviction of a police officer who passed bribes to judges of the enterprise/court); *United States v. Horak*, 833 F.2d 1235, 1239 (7th Cir. 1987) ("[C]onduct in section 1962(c) does not mean 'control' or 'manage,' . . ." Therefore, an employee of a division of a subsidiary of the charged enterprise/corporation can participate in the conduct of the corporation's affairs within the meaning of section 1962(c)); *United States v. Yonan*, 800 F.2d 164, 167 (7th Cir. 1986), *cert. denied*, 479 U.S. 1055 (1987) (attorney who bribed state prosecutors participated in the affairs of the enterprise/prosecutors' office by conducting business with it, even though he did not have a "stake or interest" in its goals).[15]

[15] As petitioners have pointed out, other circuits including at least the Second, Third, Fifth, Sixth and Ninth, articulate the participation element in slightly different words than the Seventh and Eleventh, but the results are the same: outsiders to the enterprise who affect its affairs may be reached under section 1962(c). *E.g.*, *United States v. Provenzano*, 688 F.2d 194 (3rd Cir.), *cert. denied*, 459 U.S. 1077 (1982) (owner of trucking companies liable for section 1962(c) violation where he participated in scheme to bribe an enterprise/union); *Town of Kearny v. Hudson Meadows Urban Renewal*, 829 F.2d 1263, 1266 (3rd Cir. 1987) (defendants not named in association-in-fact enterprise are still liable under section 1962(c) whether they are found to be "inside the enterprise or outside it."); *United States v. Bright*, 630 F.2d 804, 831 (5th Cir. 1980) (bonding company that bribed enterprise/sheriff's office participated in the affairs of the sheriff's office); *United States v. Elliott*, 571 F.2d 880, 903 (5th Cir.), *cert. denied sub nom. Delph v. United States*, 439 U.S. 953 (1978) ("The substantive proscriptions of the RICO statute apply to insiders and *outsiders*—those merely 'associated with' an enterprise—who participate directly *and indirectly* in the enterprise's affairs"); *United States v. Forsythe*, 560 F.2d 1127, 1136 (3rd Cir. 1977) (magistrate who accepts bribes from an enterprise/bonding company is sufficiently "associated with" the enterprise);

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It is the Seventh Circuit's construction of the statute, and not the Eighth Circuit's, that gives full effect to Congress's intent, as expressed in the words it chose for section 1962(c), that RICO reach every person who joins in an enterprise crime—insiders and outsiders alike.[16] This Court has rebuffed all attempts to read into or out of RICO requirements that do not appear in its plain language. *E.g., Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985) (holding RICO is to be "read broadly" and that "amorphous standing requirements" should not be imposed on civil RICO). There is no principled reason to read the words "or participate, directly or indirectly, in the conduct of" out of section 1962(c). To do so would eliminate liability for persons and entities who have engaged in conduct otherwise proscribed by RICO.

[15] *continued*

State of New York v. O'Hara, 652 F.Supp. 1049, 1054 (W.D.N.Y. 1987) (contractor who submitted fraudulent bids on a municipal waste clean-up contract participated in the affairs of the enterprise/city); *Virden v. Graphics One*, 623 F.Supp. 1417 (C.D. Cal. 1985) (misrepresentations of subsidiary were sufficiently related to enterprise/parent corporation to be actionable under section 1962(c)).

[16] In addition to the plain language of the statute, the legislative history of RICO also suggests that it was intended to reach beyond those who own or manage an enterprise. For example, those speaking in favor of the bill during the House debate noted it was designed to snare accounting firms, 113 *Cong. Rec.* 17949 (1967); and attorneys, accountants and business consultants. *Id.* at 17950. Both the accounting and insurance industries were specifically identified as being among those RICO was intended to reach. 116 *Cong. Rec.* 592 (1970).

D. The Litigation Floodgates Will Not Open as a Result of Adopting the Seventh Circuit's Construction of the Participation Element.

There need be no concern that an avalanche of civil RICO lawsuits will be filed if the Court adopts the Seventh Circuit's construction of "participate." Despite their success in RICO actions, insurance liquidators have been judicious in their resort to RICO. As to other RICO plaintiffs, the Seventh Circuit's construction of the participation element has been the law for more than a decade, and there is nothing to suggest that that circuit has experienced a disproportionate number of civil RICO filings.

In any event, "concern over the consequences of an unbridled reading of the [RICO] statute" is no excuse to restrict its breadth. *Sedima, S.P.R.L. v. Imrex Co., supra* 473 U.S. at 481. And, in fact, very few plaintiffs have successfully pled RICO violations against outsiders to the identified enterprise, not because of defects in their allegations regarding "participation," but because of defects regarding other elements. For example, only a very few civil RICO cases naming independent auditors and attorneys as defendants have withstood motions to dismiss in recent years, and of those, half involved situations where some or all of the alleged co-schemers had pleaded guilty to criminal charges.[17] Most have been dismissed for

[17] Reported opinions in which some or all co-schemers had pleaded guilty to criminal fraud are: *Ikuno v. Yip*, 912 F.2d 306 (9th Cir. 1990) (reversing summary judgment in favor of the attorney for a "phantom" corporation, two of whose employees had pleaded guilty to fraudulent operation of the company); and *State Farm Mutual Auto Insurance Co. v. Rosenfield*, 683 F.Supp. 106 (E.D. Pa. 1988) (attorney and doctors, who pled guilty to criminal charges of defrauding an insurance company, denied summary judgment on civil RICO claims brought by the defrauded company).

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deficiencies in the allegations of fraud,[18] pattern,[19] or enterprise.[20]

[17] *continued*

Civil RICO complaints against independent auditors and attorneys that have withstood motions to dismiss where co-schemers had not pled guilty are described in *Schacht v. Brown, supra* 711 F.2d 1343; *James v. Meinke*, 778 F.2d 200 (5th Cir. 1985) (affirming RICO jury verdict against CPA who gave clients false information when soliciting them to invest in enterprises in which he had an interest); *Gilmore v. Berg*, 761 F.Supp. 358 (D.N.J. 1991) (upholding RICO charges against attorney and accountant charged with knowingly distributing materially false information to investors in limited partnerships); *Gutfreund v. Christoph*, 658 F.Supp. 1378 (N.D.Ill. 1987) (RICO claims upheld against accountant who allegedly prepared and distributed false financial projections circulated as part of the offering materials for a limited partnership investment).

[18] *E.g.*, *Browning Avenue Realty Corp. v. Rosenshein*, 774 F. Supp. 129, 137-9 (S.D.N.Y. 1991); *Griffin v. McNiff*, 744 F.Supp. 1237, 1254-5 (S.D.N.Y. 1990); *Friedman v. Arizona World Nurseries Ltd.*, 730 F.Supp. 521, 545-6 (S.D.N.Y. 1990), *aff'd.*, 927 F.2d 594 (2nd Cir. 1991).

[19] *E.g.*, *Feinstein v. Resolution Trust Corp.*, 942 F.2d 34 (1st Cir. 1991) (attorney's representation of plaintiffs at 25 real estate closings over a period of four months insufficient to satisfy "continuity" prong of pattern requirement); *Hartz v. Friedman*, 919 F.2d 469 (7th Cir. 1990) (affirming dismissal of civil RICO pleadings against an attorney on "pattern" grounds and noting that the Seventh Circuit had not found patterns to exist in *any* civil RICO cases since this Court's decision in *H.J. Inc. v. Northwestern Bell Telephone Co.*, 492 U.S. 229 (1989)).

[20] *E.g.*, *Manax v. McNamara*, 842 F.2d 808 (5th Cir. 1988); *Bingham v. Zolt*, 683 F.Supp. 965 (S.D.N.Y. 1988) (*Turkette*-type enterprises involving attorneys, auditors and others held insufficient where there was no threat of continued illegal activity).

CONCLUSION

The participation of independent entities and consultants is essential to the ongoing operation of an insurance company. When these entities and persons join with company management to commit a pattern of racketeering activity that defrauds the company and its policyholders, they should be held accountable. To let the very persons without which the RICO scheme could not have succeeded off the hook is bad statutory construction and bad policy. For all of the reasons stated above the decision of the Eighth Circuit should be reversed.

Respectfully submitted,

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